RE: DOCKET NO. DTE01-100 (2001)

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1. **Should Massachusetts gas utilities be allowed or required to implement a risk management program to mitigate price volatility for gas customers?**

   Customer dissatisfaction and complaints caused by volatile energy bills clearly demonstrate a need for risk management programs. The Department should encourage gas utilities to offer such programs with an objective of increasing customer satisfaction. However, it is unlikely that system supply price-hedging programs would significantly increase customer satisfaction since customers would not be given a choice and volatility would not be appreciably decreased. A more effective way of achieving this objective is a voluntary fixed-bill program.[1] Such a program would offer customers a choice while eliminating volatility.

   <u>Volatile Energy Bills Cause Customer Dissatisfaction</u>

   Under traditional utility service, all customers are at risk to unpredictable prices and weather, the two factors most responsible for volatility in gas bills. Consequently, it is not surprising that many customers are confused by changes in their energy bills and feel that they lack control over them and are dissatisfied. In addition to causing dissatisfaction on the part of many customers, this volatility can create real hardships for some customers as unexpected increases cause

[1] A fixed-bill is a pre-determined annual energy bill that is offered to customers on a purely voluntary basis. Participating customers pay the same amount each month for the one-year term regardless of gas prices and weather. Unlike budget bills there is no true-up or reconciliation. All costs of the program are recovered only from participating customers through a fee contained in the fixed-bill amount. See Appendix ("A Solution to the Problem of Volatile Energy Bills") for a further description of a fixed-bill program.

them to fall behind on their payments. Extensive consumer market research also demonstrates the desire of many energy consumers to eliminate volatility from their energy bills[2].

A Voluntary Fixed-Bill Program is a Superior Means of Addressing the Problem of Volatile Energy Bills

The Department has already recognized the potential benefits of offering customers supplier choice. A voluntary risk management program recognizes the diversity of customer circumstances and preferences and can also produce benefits. In fact, voluntary fixed-bill programs generally have significantly higher enrollment and annual retention rates than supplier choice programs.

Although many customers want predictable energy bills and are willing to pay for them, others do not value predictability as highly. A voluntary program provides the customer a choice and can even increase satisfaction on the part of those customers who do not choose the service[3]. In contrast, customers have no choice regarding participation in a system supply price-hedging program.

Such a "one size fits all" approach has the potential to cause dissatisfaction since even those customers who do not value the additional stability provided by the program are forced to pay for it.

In addition, a fixed-bill program eliminates volatility instead of only reducing it. Since a fixed-bill program eliminates both price and weather related volatility, it provides the ultimate in simplicity and predictability. In contrast, system price-hedging programs and even voluntary fixed-unit price offerings are only "half-way

[2] See Appendix ("A Solution to the Problem of Volatile Energy Bills") for a description of WeatherWise's WeatherProof Bill Program and a further discussion of consumer market research.

[3] When gas bills become volatile, the availability of a fixed-bill program could mitigate the dissatisfaction of even those customers who did not select it since they made a conscious decision to take their chances on prices and the weather. The availability of this type of program would also enable the Department and the utilities to offer a solution to customers who call in with complaints about volatility.

measures" with regard to volatility[4]. Such programs reduce/eliminate price-related volatility but have no impact at all on weather related volatility. Bills remain volatile and customers remain dissatisfied. Customers who seek predictability will not be satisfied with anything less.

A fixed-bill is a significant improvement over budget bills and other level payment plans. A budget bill gives consumers an average price until the end of the year when the consumer gets a bill that can be less - or substantially more. After a cold winter or a hot summer, a budget bill can break the budget of individuals or organizations on fixed incomes. This and the fact that many customers are confused by or forget about the true-up feature of budget bills are sources of dissatisfaction. A fixed-bill program provides an alternative without these major sources of dissatisfaction.

The Department Can Encourage Utilities to Implement Voluntary Risk Management Programs by Establishing Favorable Policies and Guidelines

The Department should facilitate a clear understanding on the part of all parties of the basic nature of hedging programs. Such programs seek to reduce financial risk associated with future changes in energy prices or other inherently unpredictable variables such as the weather. Hedging is a risk mitigation tool that can reduce volatility and increase value for customers. However hedging does entail costs and although it can result in savings, it is not a cost reduction strategy per se.

[4] Considering that gas prices and weather each account for about half of the volatility in gas bills, a system supple price hedging program that hedges 25% of system supply would eliminate only about 12.5% of the volatility. It is unlikely that such a low impact program would appreciably or even proportionately mitigate dissatisfaction in the event of energy price spikes and severe weather similar to those experienced last winter.

Regulation should be light-handed in the case of voluntary hedging programs. The Department should specify general goals and parameters but leave the details to the utilities. This will encourage innovation and experimentation on the part of utilities and maximize the value for consumers.

Proposed voluntary hedging programs should receive expeditious regulatory review and approval.

The Department's policies should recognize that voluntary hedging services can and should represent "win-win" propositions for customers and utilities. A willingness to allow utilities to benefit from such programs will encourage innovation and help ensure successful implementation.

A voluntary fixed-bill program is a proven way to increase customer satisfaction. Such programs have demonstrated their ability to produce high enrollment and high customer satisfaction levels. As previously mentioned, voluntary fixed-bill programs have significantly higher enrollment and annual retention rates than supplier choice programs. In contrast, WeatherWise is not aware of any instance where a system supply price-hedging program has been shown to increase customer satisfaction.

2. How will risk-management by LDC's affect gas unbundling and customer choice in Massachusetts?

A voluntary risk management program will increase customer choice and satisfaction within Massachusetts.

3. Should gas utilities be limited to specific types of risk management instruments? If so, what type?

Utilities should not be limited to specific hedging instruments. The appropriate type of hedging instruments will depend on the specific nature of the risk management program and other factors.

4. Should there be a percentage volume of gas that LDC's would be allowed to hedge?

The percentage volume of gas that should be hedged depends on a number of factors including the type and objectives of the hedging program.

5. What should the core objectives of a hedging program be (e.g., least cost, price stability)?

The core objective of a hedging program should be to increase customer satisfaction. This can be best accomplished by:

- ?? Providing those customers who are dissatisfied with unpredictable gas bills a simple and predictable alternative
- ?? Offering an additional choice to all customers
- ?? Recovering all costs of such program only from customers who choose the service.

6. How will the Department assess risk-management programs? What benchmarks should be used to measure a risk-management program's performance?

The voluntary nature of a fixed-bill program simplifies the Department's role in assessing and reviewing the program. The Department should ensure that the communication and enrollment process is designed to increase customer satisfaction and encourage informed decision-making. In this regard, the

Department should encourage the use of accurate and concise communications materials. Overly complex communications materials will lead to confusion, dissatisfaction and high program costs. Program features and guidelines should be reviewed and approved in advance. Subsequent reviews should focus on assessing the degree of adherence to the approved guidelines.

In the case of a voluntary fixed-bill program, customer participation and satisfaction are the key benchmarks. This is best monitored by review of participation levels and annual renewal rates.

Assessments of any risk management program, whether a voluntary fixed-bill program or a mandatory system supply price hedging program should recognize the basic nature of hedging programs. Such assessments obviously should not include hindsight reviews to penalize or reward utilities based on hypothetical losses or gains as compared to actual energy spot prices of other inherently unpredictable variables. The possibility of such an assessment would understandably have a chilling effect on a utility's willingness to participate. The very concept of hedging requires a forward-looking approach. A hedging program appropriately seeks to reduce financial risk or uncertainty. In contrast, a goal of generating profits or cost savings from changes in inherently unpredictable variables is consistent with speculation, not hedging.

7. What standard of review should the Department apply to the utilities' initial risk-management program?

See the response to Question #6.

8. What types of costs are associated with risk-management? Should LDCs be allowed to recover these costs? If so, please explain how.

The costs of a voluntary fixed bill program include:

- ?? The costs of managing the financial risk associated with gas prices and weather
- ?? The costs of the communication and enrollment process
- ?? Computer system and other costs associated with developing the individualized fixed-bill quotes and performing billing and accounting functions
- ?? An amount to compensate the utility for the risk assumed under the program

Such costs should be recovered through a fee contained in the individual fixed-bill amounts. All program costs should be recovered only from participating customers.

9. Should an incentive mechanism be used in conjunction with a risk-management program? If so, please explain how this mechanism should be structured.

The Department can encourage gas utilities to offer voluntary fixed-bill programs by first recognizing that such programs can be "win-win" propositions for customers and utilities rather than merely "zero sum games." A willingness to allow utilities to also benefit from such programs will encourage innovation and help to ensure program success. In particular, the Department should allow utilities to establish fixed-bill program fees that reasonably compensate them for the risk they assume and potentially allow them to profit from successful programs.